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SUBJECT: Guangdong Toy Association 20th Anniversary -Celebration or Crisis?

REF: GUANGZHOU 618

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11. (SBU) Summary: The Guangdong Toy Association's recent Twentieth Anniversary Banquet was both a celebration of the organization's milestone, but also a rallying cry for manufacturers facing economic challenges unprecedented in the organization's history. Concerns about declining overseas orders, tight credit conditions and lasting effects of the 2007 toy safety crisis all make the industry outlook more grim than at previous annual banquets. Migrant workers, the fuel that drives this labor-intensive industry, are proving volatile if not handled properly, as demonstrated in another round of PRD toy factory layoffs and disturbances this week. Local officials throughout south China's manufacturing communities have stepped up efforts to monitor changes and prevent factory closures, and especially, labor unrest. End summary.

Happy Twentieth, But Hang On For A Bumpy Ride

12. (U) Speech after speech at the Guangdong Toy Association's twentieth anniversary dinner all cheered the industry's amazing growth from USD 1.7 billion in 1988 to USD 121.9 billion today, an increase of 87 times. However, no conversation ended without expressions of concern over the current economic conditions facing toy makers and many of south China's other labor-intensive industries. Members affirmed recent announcements that China's VAT rebates would be reinstated for many products at the same time that previously scheduled minimum wage increases would be postponed to relieve cost pressures on the manufacturing sector. On the other hand, association leaders and company representatives decried sudden and unexpected cancellations and postponements of overseas toy orders and complained about the inability to raise capital from banks and other sources.

Toy Factory Layoffs Spark Unrest

13. (U) As if another reminder of the challenges the industry faces were needed, south China newspapers and websites today showed the results of a riot by 500 laid-off workers and their sympathizers who overturned a police car and vandalized toy factory offices for Hong Kong-owned Kader Toys in Dongguan on November 25. Local officials were quick to announce that the factory had not closed and that any dispute is between a small number of laid-off employees and the managers of the model train and plush toys producer. According to

press reports, approximately 80 laid off workers objected that the size of their severance payments was as much as 50 per cent too low. The reports estimated that a total of 380 Kader employees had been laid off this month as the company worked to cut expenses. In addition to the 500 reported rioters, as many as 2000 onlookers reportedly arrived at the scene to observe the situation after word spread of the disturbance. Officials later announced that the order had been restored, although the wage dispute was not fully resolved.

Local Officials Increase Market Surveillance

¶4. (SBU) Since the high-profile failure of Smart Union Toys and subsequent labor unrest (reftel), local officials throughout the Pearl River Delta (PRD) have stepped up efforts to monitor factory conditions and help prevent further closures that might lead to social instability, according to local toy company executives. Executives from one toy manufacturer told us a vice mayor and the local labor bureau director called on their factory within days of the Smart Union closure to inquire about orders and seek assurances that the factory would not close unexpectedly or leave unpaid workers to fend for themselves. The executives found this courtesy call particularly unusual because the factory in question was a wholly-owned subsidiary of a major overseas toy maker, had been among the most stable of all local employers for more than a decade, and is located in a completely different city from the closed Smart Union factories. Widespread local and international media coverage of toy industry woes, especially on the volatile situations that erupt when unemployed workers demand back wages after unexpected factory closures, means that increased government scrutiny will continue for the foreseeable future, according to executives.

Economic Woes - Costs Increase, Orders Decline

¶5. (SBU) Mike Hou of Innomega Baby Products said Hallmark, one of his firm's largest clients, recently estimated that expenses for product safety testing in the next year would increase 30 fold. He blamed the higher costs on new testing requirements from the United States and other developed countries and said buyers would initially absorb the higher fees. Hou said that even if buyers initially paid for new, more extensive toy testing, in fact his clients' total orders would likely be reduced to help offset these additional costs. In the long term, general toy price increases will be unavoidable, according to Hou, even if oil and other commodity prices remain low and China's government slows down or suspends some of its previously announced minimum wage increases and other costly regulations.

¶6. (SBU) New orders are declining in every segment of south China's toy industry, with many citing the global economic downturn as the most important cause. When pressed, executives admit that orders for the current holiday season finished shipping months ago, and new orders for 2009 appear weak so far. Industry contacts and media reports indicate that toy orders at the most recent Canton Fair fell approximately 30 percent, further impacting the struggling toy factories in coming months. Many believe the true test will come in February and March of 2009 as factories and workers decide how to proceed after breaking for Chinese New Year at the end of January.

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